

CITY AUDITOR'S OFFICE



AUDIT OF PROFESSIONAL SERVICES CONTRACTS

Report No. CAO 2002-0102-10

June 14, 2002

RADFORD K. SNELDING, CPA, CIA, CFE

CITY AUDITOR



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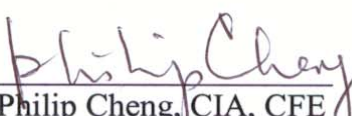
June 14, 2002

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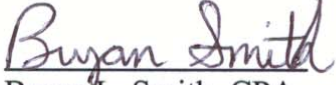
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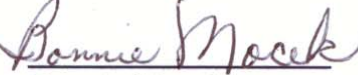
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AUDIT OF PROFESIONAL SERVICES CONTRACTS REPORT CAO 2002-0102-10

BACKGROUND

The City of Las Vegas engages various contractors to provide a wide range of professional services including architectural, engineering, consulting, financial, and legal services. Over the past three years, the City spent an average of \$9.72 million annually on professional services as shown in the following table.

Calendar Year	Professional Services Expenditures
1999	\$11.32 million
2000	\$13.56 million
2001	\$4.27 million
Annual Average (1999-2001)	\$9.72 million

Due to the nature of professional services, it is sometimes difficult to determine pricing for professional services in advance or almost impossible to only use pricing for selection. According to the Local Government Purchasing Act, professional services are not subject to the competitive bidding requirements. Currently, most of the City's professional services are acquired without the involvement of the Purchasing and Contract Division (Purchasing). Purchasing's role is limited to issuing purchase orders for professional services unless a user specifically requests assistance.

OBJECTIVES

The objective of our audit was to determine whether the City has adequate internal controls surrounding the acquisition of professional services to ensure compliance with the Local Government Purchasing Act and to prevent unfair treatment to service providers.

SCOPE AND METHODOLOGY

This audit focused on reviewing internal controls related to the existing process for acquiring professional services. The audit did not address controls surrounding construction contracts, the competitive bid process, or the purchasing of goods, as they are not directly related to

professional services. Our fieldwork was performed in accordance with generally accepted governmental auditing standards.

Our audit procedures included:

- Reviewing relevant policies and procedures, laws and regulations;
- Interviewing pertinent staff and management;
- Surveying city departments of their use of professional services;
- Reviewing service agreements and contracts;
- Analyzing purchasing transactions; and
- Examining financial records.

FINDINGS AND RECOMMENDATIONS

The City Auditor's Office appreciates the courtesy and cooperation extended to us by city employees during the audit. Our audit identified issues management should address to improve internal controls over the acquisition of professional services. These issues are summarized in the following sections. While other issues were identified and discussed with management, they were deemed less significant for reporting purposes.

1. PROFESSIONAL SERVICES POLICY AND PROCEDURES

CRITERIA:

- An organization must establish formal policy and procedures and communicate them to its employees to ensure consistency in practice and compliance with laws and regulations.

CONDITION:

- In early 1999, an audit of Purchasing identified that the City's purchasing policies and procedures needed to be updated to ensure they are current and complete.
- Over the past three years, Purchasing has been creating new citywide purchasing policies and procedures including those for professional services.
- During this audit, the professional services policy and procedures were still in draft pending final approval by the City Manager's Office. However, since the drafts have been in place for over one year, Purchasing staff were instructed by the Director of Finance and Business Services to treat them as policy.

- Most city employees involved in procuring professional services were not familiar with the professional services policy and procedures created by Purchasing.
- Our review of the draft policy and procedures for professional services identified the following deficiencies:
 - The term “professional services” is not clearly defined to assist users in determining what specific types of services need to comply with the policy and procedures.
 - The policy and procedures do not specify when a service contract/agreement is required, whether all contracts need to be reviewed and approved by the City Attorney’s Office, and who has the authority to sign a professional services contract on behalf of the City.
 - The policy document states that departments may prepare and issue contracts for professional services without the involvement of Purchasing.

EFFECT:

- Inconsistent practices in procuring professional services.
- Potential violations of Nevada Revised Statutes (NRS) Local Government Purchasing Act.

CAUSE:

- Professional services policy and procedures have not been formally reviewed and authorized by the City Manager’s Office and implemented throughout the City.

RECOMMENDATIONS:

1. Purchasing should review, finalize, and seek formal approval of its professional services policy and procedures.
2. Once the professional services policy and procedures are authorized, Purchasing should formally notify and require all city departments to adopt and comply with the approved policy and procedures.

2. APPLICATION OF PROFESSIONAL SERVICES POLICY

CRITERIA:

- To ensure compliance with an established policy, the policy maker should provide guidance to the users and specify the circumstances under which the policy applies.

CONDITION:

- According to NRS 332, professional services are exempt from the public bid requirements. However, NRS is silent on the definition of professional services.
- In Purchasing's draft professional services policy, the term "professional services" is defined as:
 - Services rendered requiring scientific knowledge or professional skill which are predominately mental or intellectual.
 - Services requiring personal services which demand extraordinary skill, experience, technical learning and/or business judgment of a specialized character.
 - Services which require the use of creative and individual talents or unique artistic skills that far outweigh monetary considerations in determining the service provider."
- In our discussion with the users of professional services, many employees expressed concerns that there is a lack of guidance as to what constitutes professional services and thus may exempt a contract from public bid without violating NRS.
- During the audit, we identified the following instances of confusion on the application of the professional services policy and procedures:
 - Similar services are classified as professional service contracts by one department and non-professional by another; and
 - Instances of disagreement between Purchasing and city departments as to whether a service is professional or non-professional.
- According to the City's chart of accounts, sixteen categories of services are listed under the "Professional Services" series. However, it is questionable whether some services listed in this series align with Purchasing's definition of professional services. On the other hand, other services (e.g. advertising, printing, billings and collections) are not listed within the "Professional Services" series but are often classified as professional services by the users.

EFFECT:

- Potential violation of NRS.

CAUSE:

- NRS is silent on the definition of "professional services".
- Purchasing has not clearly defined what constitutes professional services.
- There is a lack of guidance for users to determine what services are subject to the professional services policy and procedures.

RECOMMENDATIONS:

1. Purchasing should provide clear guidance to city departments to assist them in determining what services qualify as professional services and are therefore exempt from public bid and what services are subject to public bid.
2. Purchasing should prepare a list of commonly used services that would qualify as professional services and make the list available to all city departments. The list should be updated periodically.
3. City departments should consult Purchasing if they are uncertain as to whether certain services should be classified as professional services. This requirement should be incorporated into the professional services purchasing procedures.
4. Purchasing should meet with Accounting to determine if the chart of accounts for professional services could be more closely aligned with the definition of professional services.

3. SELECTION AND EVALUATION OF SERVICES PROVIDERS

CRITERIA:

- Proper controls surrounding the selection and evaluation of services providers reduce potential conflicts of interest.

CONDITION:

- According to the draft professional services policy, city departments may enter into contracts for professional services without the involvement of Purchasing.
- Purchasing is only involved in the pricing and/or vendor selection of professional services contracts when requested by city departments.
- Over the past three years, city departments have engaged more than six hundred contractors for professional services. The majority of these services were acquired without Purchasing's active involvement.
- Without the scrutiny of Purchasing, the only controls surrounding the procurement of professional services are departmental supervisory review and budgetary controls.
- Purchasing has not established a formal process for evaluating the performance of service providers.
- During our audit, we requested that city departments identify all professional services they had contracted in 2001. Based on our discussions with the service users and our review of the available services contracts, the following control weaknesses were noted:

- Many services providers were selected without pre-established selection criteria or an independent evaluation team;
- Users did not consistently document their basis for identifying, determining, and selecting service providers;
- Users did not make sufficient efforts to identify or contact potential service providers; and
- City departments have retained service providers and deemed the contractor as sole source without adequate explanation or justification.

EFFECT:

- City employees may be involved in potential conflicts of interest.
- Potential additional costs to the City.

CAUSE:

- Staff constraints in Purchasing.
- Lack of formal instructions provided for city departments.
- Lack of planning by city departments.

RECOMMENDATIONS:

1. Purchasing should establish adequate controls to ensure professional services are acquired in compliance with the City's policy and procedures.
2. A service provider selection form should be designed by Purchasing for use by city departments to document their basis for selecting a service provider.
3. If a service provider is deemed to be sole-source by the user department, detailed explanation and justification should be provided to Purchasing.
4. Employees responsible for ranking/selecting service providers should be provided and sign a disclosure form to help identify potential conflicts of interest.
5. Purchasing should design a generic contractor performance evaluation form for use by city departments to document the performance of service providers on an annual basis. City departments may customize the generic form to meet their specific needs and should consider the evaluation in the future selection of service providers.
6. Management of city departments should be required to review and approve all service provider selection, sole-source justification, conflicts of interest disclosure, and contractor performance evaluation before sending the forms to Purchasing.

4. SELECTION COMMITTEE OVERSIGHT

CRITERIA:

- Proper oversight over the selection of service providers protects against favoritism and unfair treatment.

CONDITION:

- A significant number of the City's professional services contracts are with various professional engineering and architectural firms for public works projects.
- The Public Works Department requests Statements of Qualifications (SOQ) biannually from these firms.
- Evaluation teams for the various service categories are established to evaluate the SOQs and the firms are ranked according to scores given by the teams. In addition, the firms are evaluated as to whether they are best suited for large or small projects.
- As public works professional services projects arise, a selection committee comprised of Public Works upper management uses the rankings to select firms for the projects. While the selection committee tries to follow the rankings in assigning projects, they have discretion in their selections in an effort to assign firms best suited for the projects. Minutes are maintained of the selection committee meetings.
- Currently, the acquisition of public works professional services is handled by the Public Works Department without Purchasing's involvement.
- No formal oversight exists over the selection committee.

EFFECT:

- Potential unfair treatment towards certain firms by the selection committee.

CAUSE:

- Need for additional level of oversight not considered necessary.

RECOMMENDATIONS:

1. Copies of the minutes of the selection committee should be forwarded by Public Works to both Purchasing and the City Manager's Office for review.
2. Annual reconciliation of firms selected for projects to SOQ rankings should be created and forwarded by Public Works to Purchasing and the City Manager's Office for review.

5. PROFESSIONAL SERVICES CONTRACT

CRITERIA:

- Due to the nature of professional services, various factors like timing and scope of work affect the pricing of service. Deliverables need to be specified to ensure performance and completion of services. It is essential to stipulate service terms and conditions in a service contract or agreement.

CONDITION:

- According to the “Vendor’s Guidebook” published by Purchasing, professional services are acquired with a purchase order and a contract. However, there is no control in place to ensure all professional services are acquired with a contract.
- Currently, Public Works uses “boiler-plate” terms and condition as standard clauses for its architectural and engineering contracts.
- In discussions with the City Attorney’s Office, we determined that department directors and the City Manager’s Office were advised through a memorandum, “any project which involve a legal or a quasi-legal matter should be brought to the attention of the Office of the City Attorney.”
- The City Attorney’s Office advised initiating departments to include a line following the signature line of the Mayor which states, “Approved as to form: (and a signature line and date for the Assistant City Attorney)”. The City Attorney’s Office further advised that their review was to legal form only.
- In our discussion with users of professional services throughout the City, many stated that some professional services, especially those of low dollar value, were acquired without a contract or precise specification of terms and conditions. They were uncertain as to when a contract is required.
- Many users were unaware of the policy of the City Attorney’s Office and were uncertain as to when a contract should be submitted to the City Attorney’s Office for review and approval.
- In our discussions with the users, it was generally assumed that the attorney had reviewed the contract as to substance and business terms instead of just as to form.
- Currently, only a few city officials are authorized to execute a contract on behalf of the City. They include the Mayor, City Manager, Purchasing and Contracts Manager, Finance and Business Services Director, Public Works Director, and Field Operations Director.

Audit of Professional Services Contracts

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May 23, 2002

- Some professional services contracts, especially those with low dollar value (under \$25,000), were signed by employees without signing authority.
- We reviewed a sample of professional services contracts and noted the following deficiencies:
 - Scope of work and deliverables were not always clearly stated;
 - Lack of specifics for pricing arrangements and cost escalation provisions; and
 - Absence of standardized clauses such as hold-harmless clause, insurance requirement, right to audit clause, etc.

EFFECT:

- Potential financial or legal liabilities.

CAUSE:

- Formal professional services policy and procedures have not been implemented and enforced.
- Many users are not aware of the City Attorney's role and responsibilities in reviewing contracts.

RECOMMENDATIONS:

1. Purchasing should provide specific guidance with regard to contract requirements for the acquisition of professional services.
2. The City Manager's Office should further emphasize the role and responsibilities of the City Attorney's Office in reviewing professional services contracts.
3. Purchasing should work with the City Attorney's Office to create "boiler-plate" contracts for frequently used professional services by city departments.
4. City departments should be required to forward all professional services contracts to Purchasing for retention.

6. BUSINESS LICENSE REQUIREMENT

CRITERIA:

- According to the City's Municipal Code, a person or business is required to obtain a valid business license if it commences, carries on, or engages in any business, either permanently or temporarily, within the corporate limits of Las Vegas. Generally, provision of a service is as relevant to this requirement as the provision of a product or a commodity.

CONDITION:

- Businesses of non-professional services are required to have and show evidence of a city business license during the bid process.
- However, since most of the professional services do not go through the bid process, city departments are less likely to request the service providers to produce business license evidence.
- Our review of a list of professional services providers over the past three years indicated that more than 500 contractors did not obtain any city business license while providing professional services to the City.
- According to Municipal Code 6.04.060, the annual business license fee for professionals such as accountants, architects, attorneys, and engineers is \$200.

EFFECT:

- Potential violation by the City of the city ordinance of business licensing requirement.
- Loss of business license revenues.

CAUSE:

- Lack of internal controls to ensure all service providers have the appropriate city business license(s).

RECOMMENDATION:

1. Purchasing and Business Licensing should develop controls to ensure city departments only engage contractors with the required city business license for professional services.

MANAGEMENT RESPONSES

1. PROFESSIONAL SERVICES POLICY AND PROCEDURES

RECOMMENDATION 1

Management Plan of Action and Timetable:

A new city wide process for drafting, reviewing, and approving policies and procedures has been delayed due to an administrative reorganization. Consequently, the Finance Department will take the initiative to disseminate department draft documents for review and comment, and ask that the City Manager approve into formal implementation. The Finance Department expects this can be accomplished by June 30, 2002.

RECOMMENDATION 2

Management Plan of Action and Timetable:

The dissemination vehicle will be the department's Tribune Intranet web site, and other departments will be expected to print and disseminate copies as needed to those who do not have Intranet access. The Finance Department expects this can be accomplished by June 30, 2002.

2. APPLICATION OF PROFESSIONAL SERVICES POLICY

RECOMMENDATION 1

Management Plan of Action and Timetable:

Management is reluctant to define professional services more stringently than the Nevada Revised Statute because we believe the Nevada Legislature purposely provided discretion to the local government. There are several Nevada Attorney General opinions that have been used to frame the definition, and we believe that definition coupled with guidance from the Purchasing & Contracts Division and the addition of examples to the policy statements are sufficient for this purpose. The Policy will be clear about who has the final authority to determine professional services. The Finance Department expects the policy will be published by June 30, 2002.

RECOMMENDATION 2

Management Plan of Action and Timetable:

Management does not want to provide a list of commonly used services, but does agree that examples would be helpful. The Finance Department expects this can be accomplished by June 30, 2002.

RECOMMENDATION 3

Management Plan of Action and Timetable:

The requirement to consult with Purchasing and Contracts when uncertainty exists about the determination of professional services will be added to the procedures. The Finance Department expects this can be accomplished by June 30, 2002.

RECOMMENDATION 4

Management Plan of Action and Timetable:

The Purchasing and Accounting Division have determined that the chart of accounts would not help identify PSAs. Instead, Purchasing will preface the Oracle purchase order header with the prefix, "PSA". From this prefix, we can run reports to identify PSA's for future review and audits. The prefacing of purchase order headers will be accomplished by June 14, 2002.

3. SELECTION AND EVALUATION OF SERVICES PROVIDERS

RECOMMENDATION 1

Management Plan of Action and Timetable:

The Purchasing & Contracts Division concurs with the recommendation, and anticipates implementation by June 30, 2002.

RECOMMENDATION 2

Management Plan of Action and Timetable:

The Purchasing & Contracts Division concurs with the recommendation, and anticipates implementation by June 30, 2002.

RECOMMENDATION 3

Management Plan of Action and Timetable:

The Purchasing & Contracts Division concurs with the recommendation, and anticipates implementation by June 30, 2002.

RECOMMENDATION 4

Management Plan of Action and Timetable:

The Purchasing & Contracts Division concurs with the recommendation, and anticipates implementation by June 30, 2002.

RECOMMENDATION 5

Management Plan of Action and Timetable:

The Purchasing & Contracts Division concurs with the recommendation, and anticipates implementation by June 30, 2002.

RECOMMENDATION 6

Management Plan of Action and Timetable:

The Purchasing & Contracts Division concurs with the recommendation, and anticipates implementation by June 30, 2002.

4. SELECTION COMMITTEE OVERSIGHT

RECOMMENDATION 1

Management Plan of Action:

We will forward copies of Selection Committee minutes to Purchasing and City Manager's Office.

Timetable:

We will forward minutes the next time the Committee meets and every time after that.

RECOMMENDATION 2

Management Plan of Action:

An annual reconciliation will be created and forwarded to Purchasing and City Manager's Office.

Timetable:

We will do so at the end of the year. We may find that a reconciliation is more appropriate at the end of two years, because the ranking list is good for two years but there is nothing wrong with one year.

5. PROFESSIONAL SERVICES CONTRACT

RECOMMENDATION 1

Management Plan of Action and Timetable:

Concur, pursuant to Management Responses to RECOMMENDATIONS 1, 2, and 3. Action should be implemented by June 30, 2002.

RECOMMENDATION 2

Management Plan of Action and Timetable:

We concur with the recommendations of the Auditor. Prior to her departure, Virginia distributed a memo to all department directors which included three previous memos distributed from the City Attorney between 1993 and 1995. In her memo, she has asked directors to be aware of these procedures and to share them with related staff. I believe that this memo provides the emphasis needed. We will also visit this topic in our Executive Management Meetings.

RECOMMENDATION 3

Management Plan of Action and Timetable:

Concur. Purchasing shall submit templates by June 30, 2002 for City Attorney review.

RECOMMENDATION 4

Management Plan of Action and Timetable:

The Purchasing and Contracts Division is proposing a matrix approach that will require the Division establish the policy, procedure, forms, and guidelines, and allow for some authority on the part of department management to enter into professional service agreements. Action should be implemented by June 30, 2002. The procedure will require departments and divisions forward their contract documentation for those less than or equal to \$25,000 to the Purchasing & Contracts Division for retention. The City Clerk and/or the Purchasing & Contracts Division currently retain contracts in excess of \$25,000.

6. BUSINESS LICENSE REQUIREMENT

RECOMMENDATION 1

Management Plan of Action and Timetable:

The Purchasing & Contracts and Business Services divisions implemented a process to verify business licenses for all firms and individuals who are seeking contracts with the City in excess of \$25,000. This program has been very successful. Due to the fact that Purchasing & Contracts does not get involved with contracts at or below \$25,000, verification has not been taking place. The revised policy and procedure will require requesting departments, as part of completing the template for source justification documentation, to obtain the City business license number from the selected source. If one is not provided, the department will be instructed to confer with the Business Services Division to determine if one is needed. Many consultants perform work outside of Las Vegas and deliver documents by mail or email, or sub-contract their work to local businesses that may already have city business licenses. In those cases, Municipal Code may not require these consultants to have City business licenses. Action should be implemented by June 30, 2002.